

*The purpose of this report is to keep policy makers apprised of changes in
the national and local economies that
the Montgomery County Department of Finance
believes may impact current and/or future revenues and expenditures.*

*This report is also available through the Internet
on the Montgomery County Web Page:
<http://www.montgomerycountymd.gov>*

For questions regarding this report, please contact:

*David Platt
Chief Economist
Montgomery County Department of Finance
101 Monroe Street, 15th Floor
Rockville, Maryland 20850*

*Phone: (240) 777-8866
Email: David.Platt@montgomerycountymd.gov*

INTRODUCTION

This quarterly report provides an analysis of national, regional, and Montgomery County economic indicators for the first quarter of 2014 and forecasts of selected national indicators. The data presented in this report are not seasonally adjusted to insure comparability among the national, regional and Montgomery County economic indicators. Since the data are not seasonally adjusted, the comparative periods are the first quarter of this year and the first quarter of 2013. The only data that are seasonally adjusted are the national gross domestic product (GDP) and its components.

NATIONAL ECONOMY

According to the Bureau of Economic Analysis (BEA), U.S. Department of Commerce, gross domestic product (GDP) decreased at a 1.0 percent seasonally adjusted annual rate during the first quarter of 2014. That decrease followed seventeen out of eighteen quarters of growth since the end of the recession in June 2009. Based on the May *Wall Street Journal (WSJ)* survey of fifty economists, the average of the responses expect economic growth to increase 3.0 percent during the current second quarter, 3.0 percent during the third quarter, and 3.1 percent during the fourth quarter. The survey of economists expects the jobless rate to be at 5.6 percent by December and 5.4 percent by December 2015. The result of the survey of economists shows that inflation pressures, as measured by the consumer price index (CPI), will remain below 2.0 percent throughout 2014 and 2015.

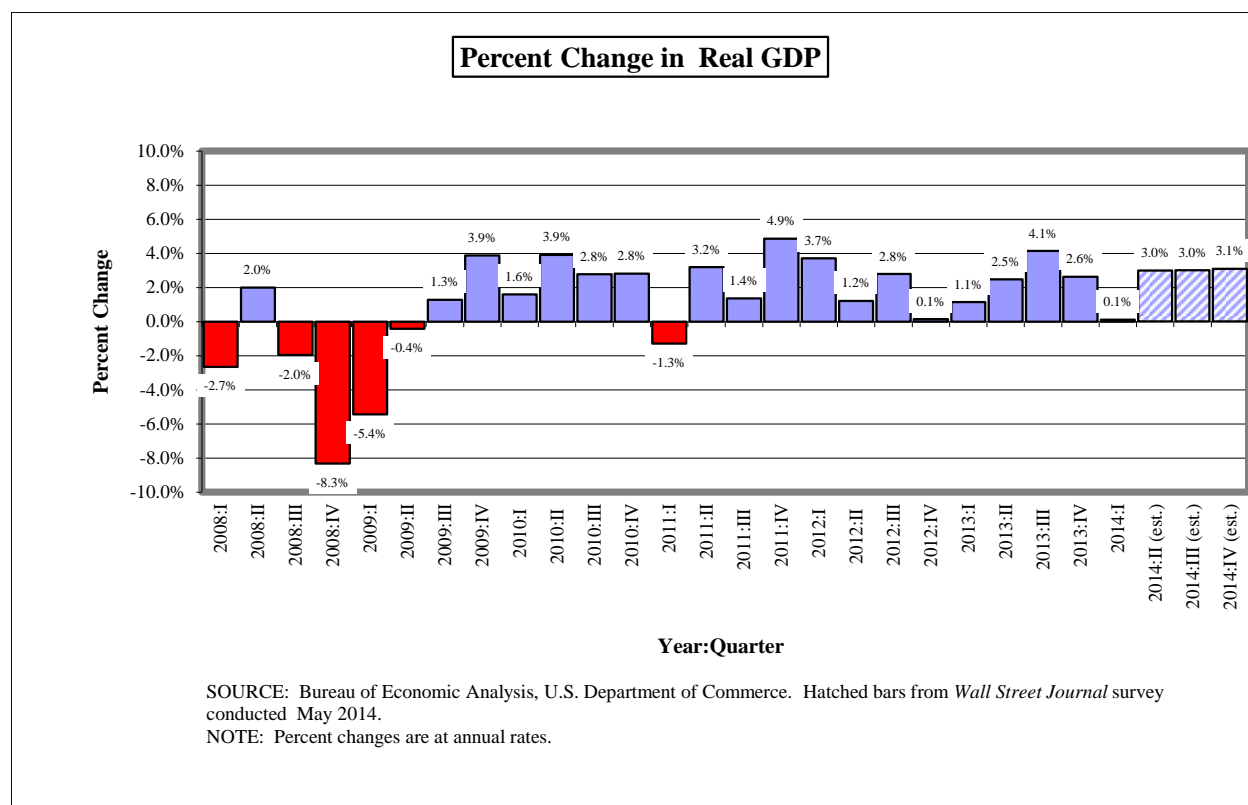
According to the second quarter survey of professional forecasters conducted by the Federal Reserve Bank of Philadelphia, “forecasters see stronger quarterly growth this year accompanied by lower unemployment.” According to forty-two forecasters surveyed, economic growth during the second quarter will be 3.3 percent at an annual rate, third quarter growth will be 2.9 percent, and fourth quarter growth will be 3.2 percent. The forecasters predict that the unemployment rate will be an average of 6.4 percent in 2014, declining to 5.9 percent in 2015, 5.6 percent in 2016, and 5.5 percent in 2017. Finally, the forecasters predict that the second quarter CPI will average 1.9 percent, followed by 1.9 percent in the third quarter, 2.0 in the fourth quarter, and 2.0 percent in the first quarter of 2015.

Overall, both surveys expect economic growth to range between 2.9 percent and 3.3 percent through the remainder of 2014 while inflation continues to remain subdued at or below 2.0 percent.

Subsequent to its April 29-30 meeting of the Federal Open Market Committee (FOMC, Committee) of the Board of Governors of the Federal Reserve System, the Committee stated that “economic activity has picked up recently, after having slowed sharply during the winter in part because of adverse weather conditions.” While labor market indicators showed improvement, “the unemployment rate remains elevated.” The Committee “reaffirmed its view that a highly accommodative stance of monetary policy remains appropriate.” The Committee will maintain the current 0 to $\frac{1}{4}$ percent target range for the federal funds rate and assess progress towards its dual mandate of maximum employment and 2 percent inflation

Both the WSJ April survey of economists, the Philadelphia survey of professional forecasters, and the economic projections by the FOMC in March suggest that unemployment will gradually decrease to 5.4-5.6 percent by the end of 2016 and inflation, as measured by either the CPI or the PCE indices, will increase slightly to 2.0 percent (both CPI and PCE), suggesting that inflation will remain subdued over the next three years while unemployment will decrease.

Data released by BEA for the first quarter showed that the modest increase in real GDP was attributed to an increase in personal consumption expenditures ($\uparrow 3.0\%$ - down from the $\uparrow 3.3\%$ during the fourth quarter of last year) that were offset by declines in exports ($\downarrow 7.6\%$ - compared to the $\uparrow 9.5\%$ during the fourth quarter), nonresidential fixed investment ($\downarrow 2.1\%$ compared to $\uparrow 5.7\%$ during the fourth quarter), and second consecutive decline in residential fixed investment ($\downarrow 5.7\%$). The deceleration in the first quarter reflected a decline in private inventory investment which subtracted 1.01 percent point from the first-quarter change in real GDP after adding 0.41 percentage points to the fourth-quarter change of 2.6 percent.

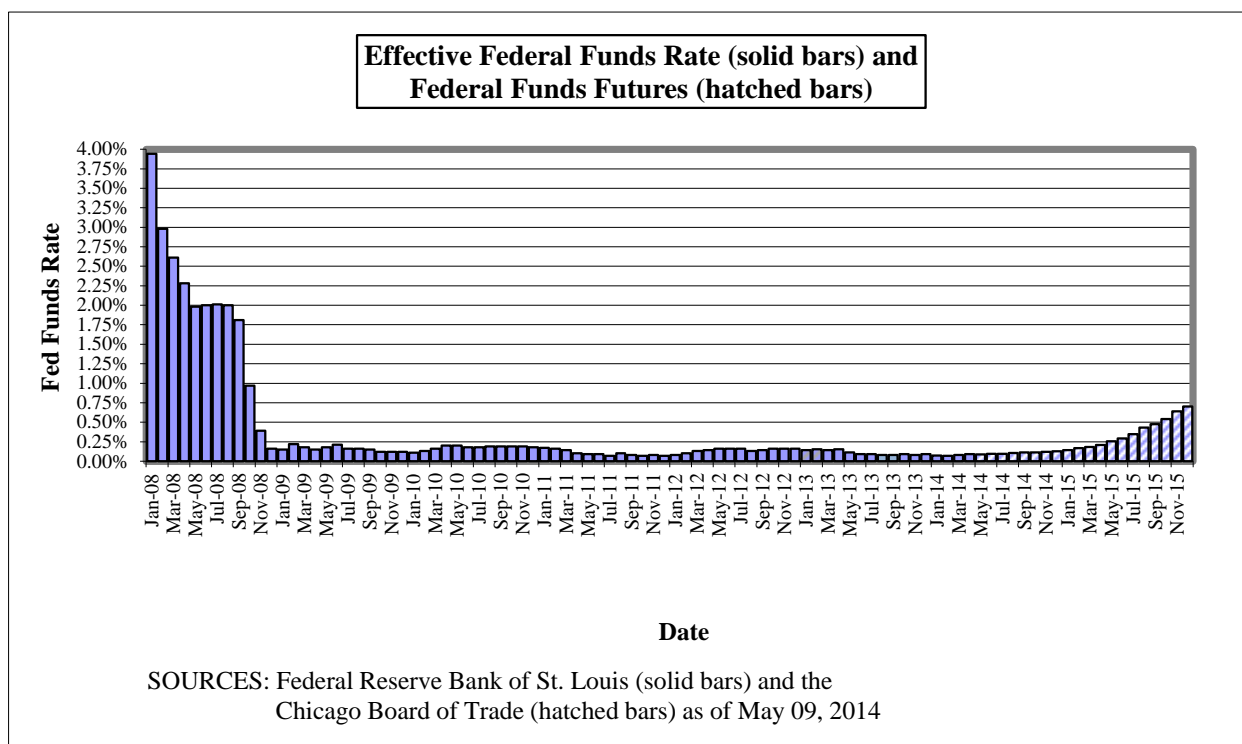


Real final sales of domestic product, which measures aggregate demand and is GDP less the change in real private inventories, increased 0.7 percent during the first quarter compared to 2.7 percent during the fourth quarter. Real final sales are a good measure of future production. If the growth rate in real final sales exceeds the growth rate for GDP over an extended period of time, it indicates strong demand and an expansion of the national economy.

Following its meeting on April 29 and 30, the FOMC stated in its press release that “the Committee reaffirmed its view that a highly accommodative stance of monetary policy remains

appropriate. In light of the cumulative progress toward maximum employment and the improvement in the outlook for labor market conditions, the Committee decided to make a further measured reduction in the pace of its asset purchases. Beginning in May, the Committee will add to its holdings of agency mortgage-backed securities at a pace of \$20 million per month and will add to its holdings of longer-term Treasury securities at a pace of \$25 million per month.”

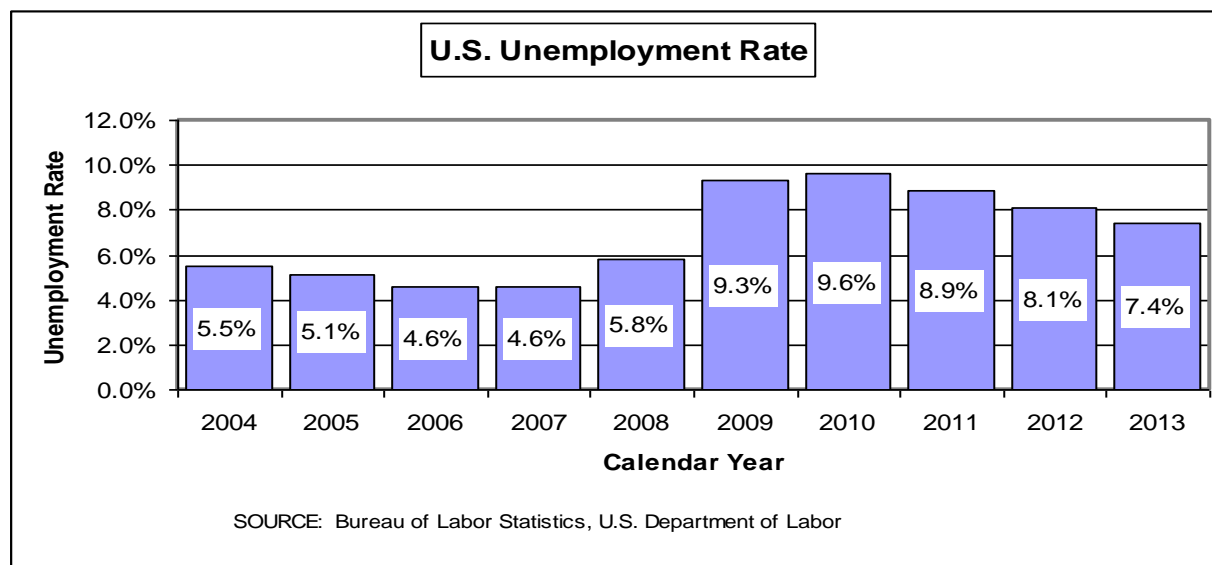
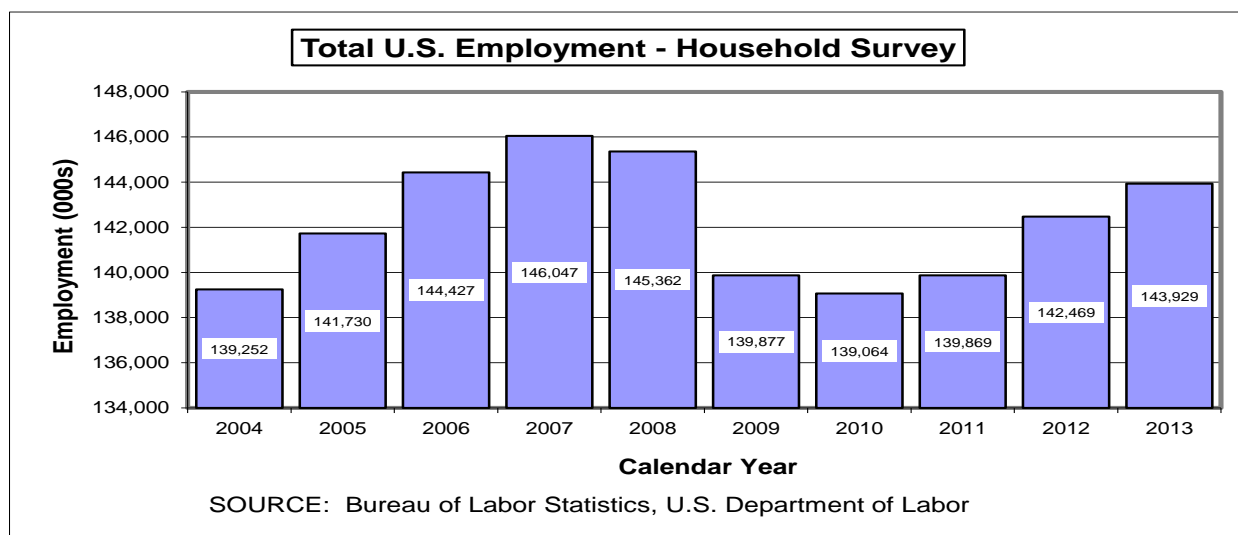
Since the April meeting of the FOMC, the futures market for the 30-day federal funds rate remains at or below the 0.25 percent level through May 2015. After that date, the futures market expects the rate to gradually increase to nearly 0.70 percent by the end of 2015. Following its March meeting, the FOMC released its latest economic projections through 2016. The average of responses from four members of the Board of Governors and fourteen presidents of the Federal Reserve Banks indicated increasing the target federal funds rate to 1.13 percent in 2015 and 2.42 percent in 2016. While the increase in 2015 exceeds that of the federal funds futures market, it should be noted that all of the responses ranged from 0.25 percent to 3.00 percent while the majority of responses ranged between 0.25 percent and 1.00 percent.



Sales of existing homes decreased 6.6 percent during the first quarter of this year compared to the first quarter of 2013. That decline is the first such decrease since the first quarter of 2011 (↓0.5). Even with that decline, sales during the first quarter were the second highest quarterly sales since 2009. Median home prices for existing homes increased 8.9 percent during the first quarter of 2014 compared to an 11.1 percent increase during the same period in 2013. The inventory-to-sales ratio for new homes for sale dropped to a 4.9-month inventory in 2013 from

5.9-month inventory the previous year. The inventory level increased 3.0 percent during the first quarter but was the second lowest in the past eight years.

Monthly national employment, as measured by the survey of households, averaged 144.3 million during the first quarter of this year – an increase of 1.46 percent from the first quarter of 2013 but slightly below the 144.7 million peak during the first quarter of 2007. Employment reached slightly more than 143.9 million in calendar year 2013 – an increase of 1.02 percent from calendar year 2012. However, employment in 2013 was 2.2 million below the peak employment in 2007. The unemployment rate during the first quarter stood at 6.9 percent and a significant decline from the 8.1 percent in the first quarter of 2013. After peaking at 9.6 percent in calendar year 2010, the unemployment rate steadily declined to 7.4 percent in 2013.

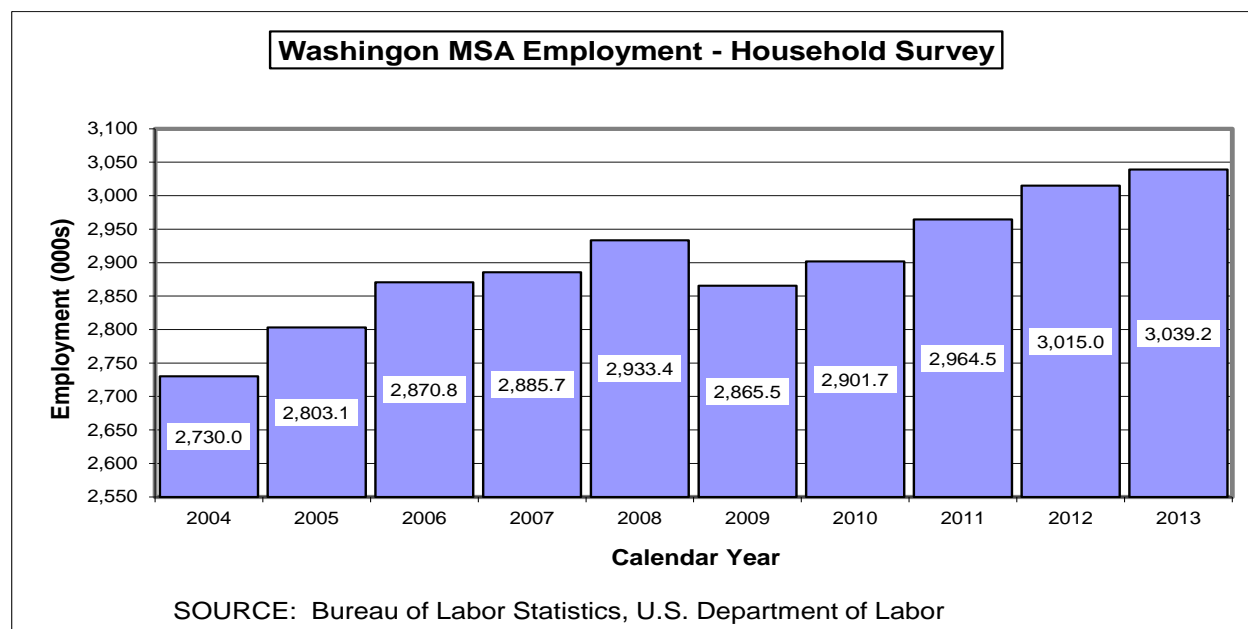


After experiencing strong performance in 2013, the stock market retreated to lower growth rates during the first quarter of 2014. All four stock market indices – the Dow-Jones Industrial Average ($\downarrow 0.72\%$), the Standard & Poor's 500 ($\uparrow 1.30\%$), the NASDAQ ($\uparrow 0.54\%$), and the Russell 2000 ($\uparrow 0.81\%$) – experienced either weak performance and, in the case of the DJIA, a decline. The question is whether the first quarter performance portends a weak stock market in 2014. Based on data since 1998, there is a modest correlation or association between first quarter and annual returns for the DJIA, NASDAQ and S&P 500 indices. However, there is very little correlation or association for the Russell 2000 index. Therefore, first quarter returns do not provide any insight as to the performance of the stock market in 2014.

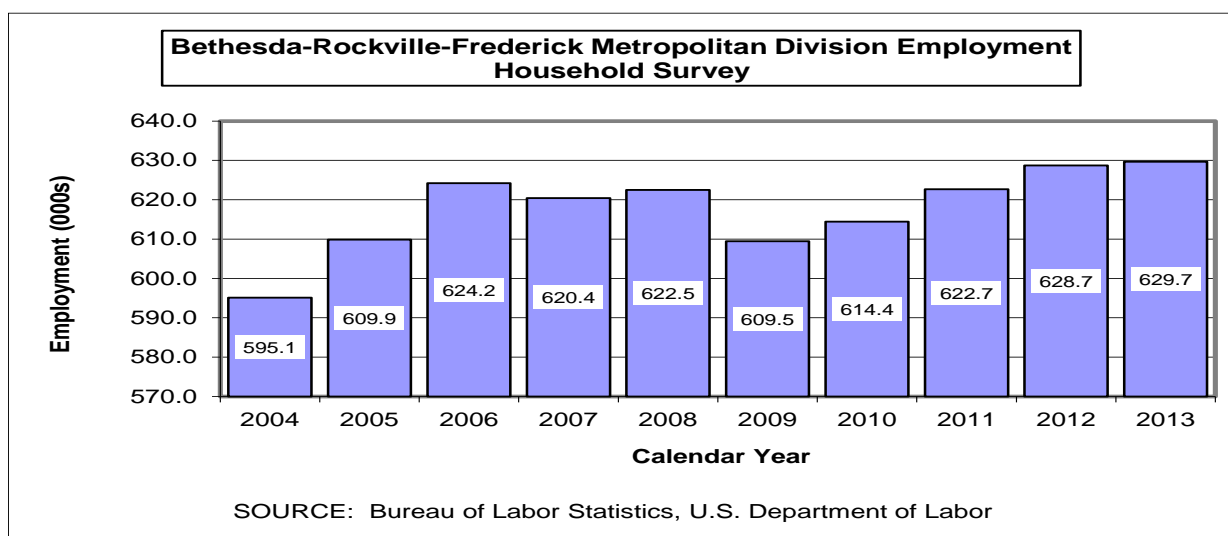
The strength of the stock market since its nadir in March 2009 has been attributed in part to the policies of the Federal Reserve and its asset purchasing program. Since the Federal Reserve began its three “quantitative easing” programs in March 2009, their affect on stock market returns has been significant. For example, starting with the first “quantitative easing” program in March 2009, the DJIA increased over 71 percent until its suspension in April 2010. Starting with the second “quantitative easing” program, the DJIA increased over 24 percent between August 2010 and June 2011. Therefore as the Federal Reserve continues to reduce its asset purchasing program through October of this year given the current reduction schedule, and the uncertain geopolitical and global financial and economic crises, the stock market may experience periods of volatility from month to month during the calendar year.

REGIONAL ECONOMY

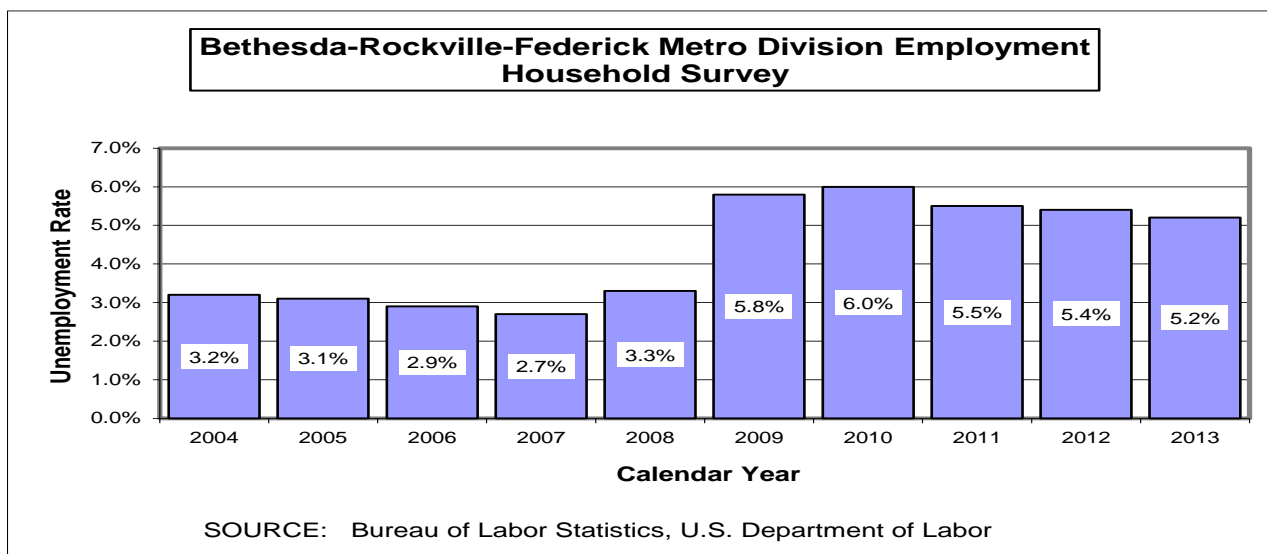
According to the employment data from the Bureau of Labor Statistics, U.S. Department of Labor and based on the household survey, monthly employment in the Washington area averaged 3,056,700 during the first quarter of 2014 – an increase of 1.2 percent from the first quarter of 2013. In 2013, employment in the Washington area increased 0.8 percent from 2012 and reached its highest level ever.



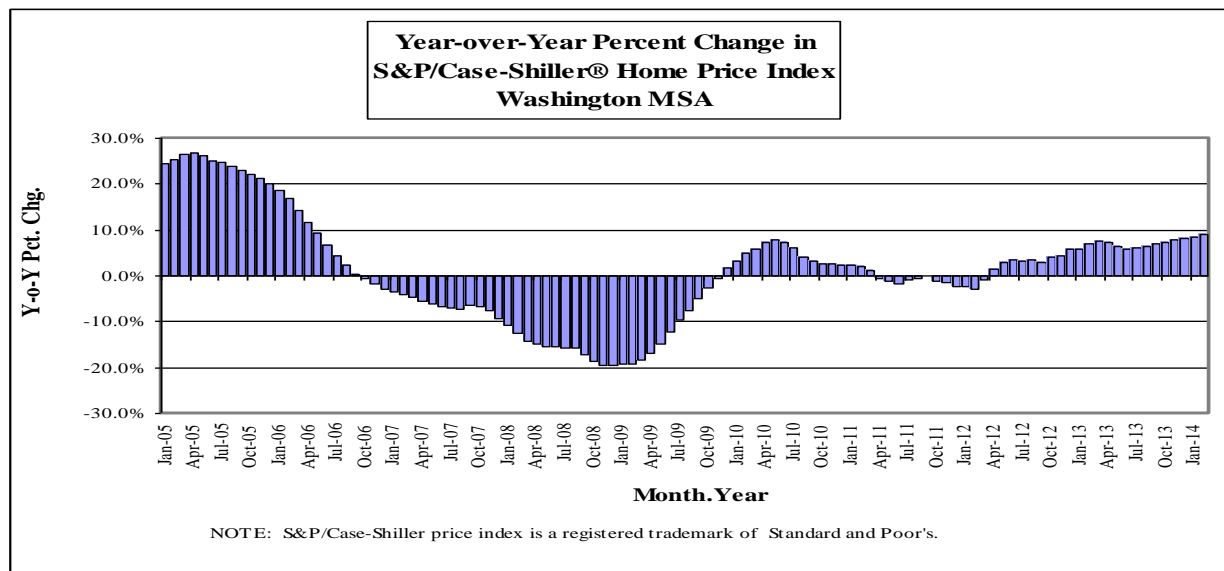
Monthly employment for the Bethesda-Rockville-Frederick (BRF) metropolitan division averaged nearly 627,100 during the first quarter and was slightly above employment in the first quarter of 2013 ($\uparrow 0.04\%$). That rate of growth is significantly lower than the first quarter growth rate for the entire Washington MSA ($\uparrow 1.2\%$). Employment for the metropolitan division barely increased in 2013 from 2012. According to the BLS data, employment for individuals residing in Montgomery and Frederick counties increased a meager 1,000 or less than 0.2 percent. However, despite that modest increase, employment reached its highest level ever in the Bethesda-Rockville-Frederick metropolitan division



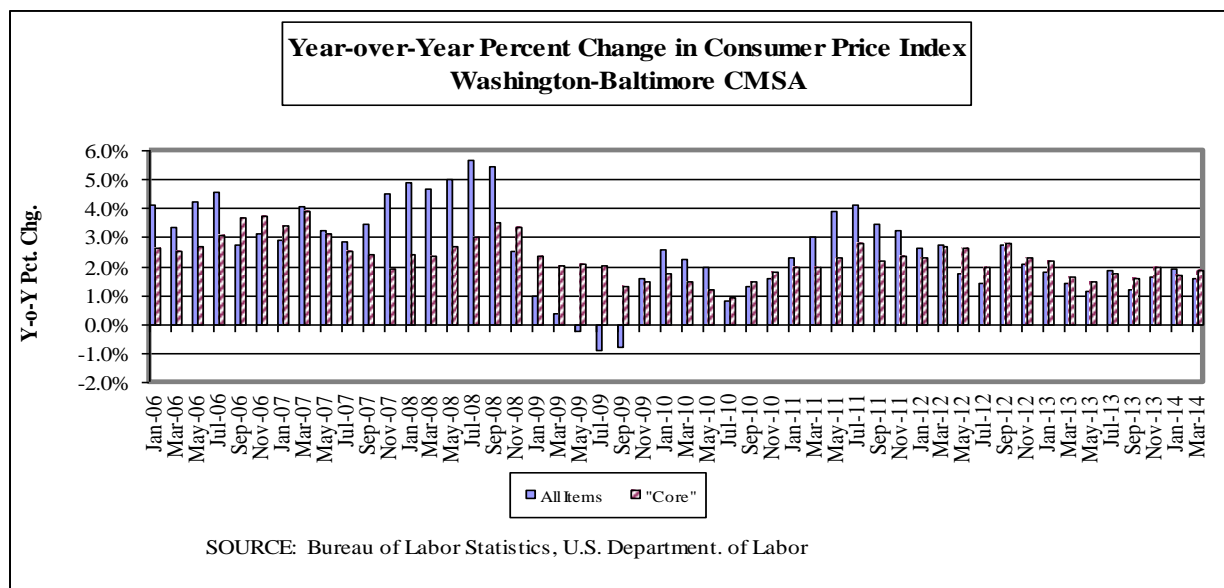
Yet even with its less than stellar employment growth in the metropolitan division during 2013, the unemployment rate for the division is either the lowest or one of the lowest among the 34 national metropolitan divisions and the monthly average was 4.6 percent during the first quarter.



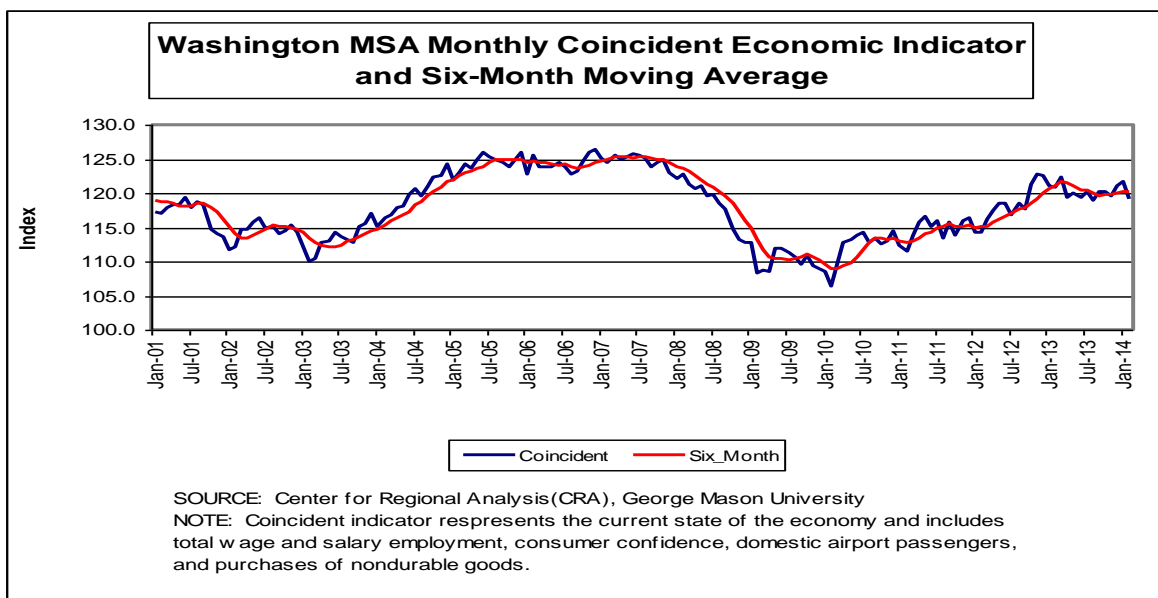
The resale housing market across the region experienced growth in prices, on a year-over-year basis, between February 2013 and February of this year. Based on the S&P/Case-Shiller® Home Price Index for the Washington region, prices in February increased 9.1 percent over the twelve-month period.



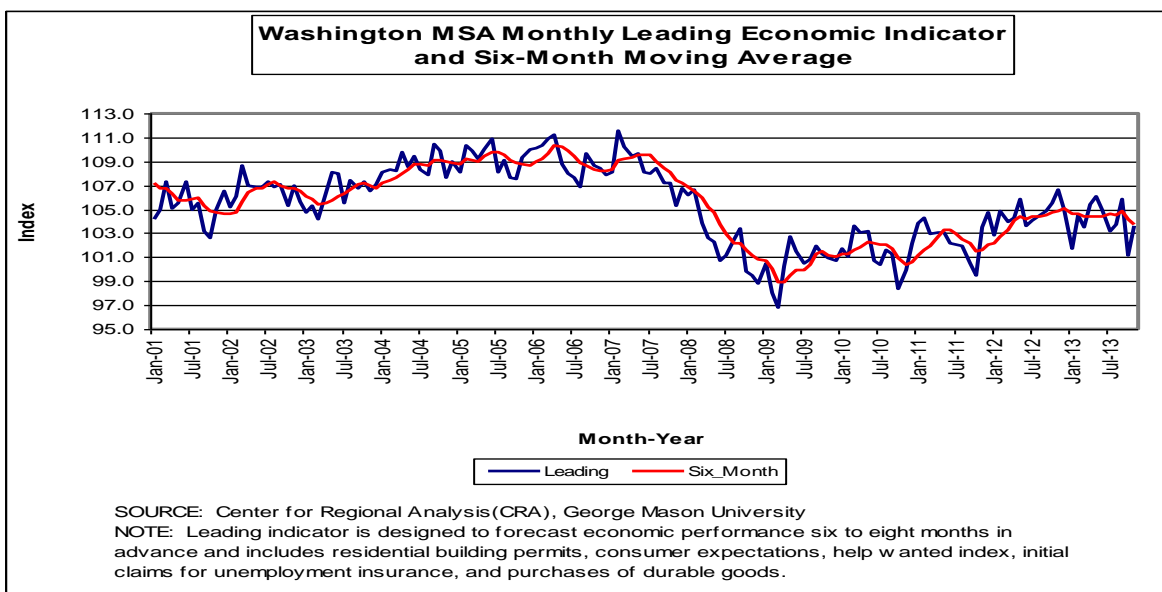
As measured by the Consumer Price Index for All Urban Consumers (CPI-U), inflation in the Washington-Baltimore region increased 1.6 percent on a year-over-year basis in March of this year over March 2013. Consumer prices excluding food and energy purchases were up 1.9 percent in the region (on the same year-over-year basis).



According to the Center for Regional Analysis (CRA) at George Mason University, the monthly coincident economic indicator for the Washington metropolitan region decreased 2.1 percent in February over January and decreased 1.5 percent over February of 2013. The coincident index measures the current performance of the region's economy. However, since reaching its lowest point in February 2010, the index increased 12.0 percent through February.



However, while the coincident indicator decreased in February, CRA also reported that the leading economic indicator increased 1.7 percent in February over January and increased 4.5 percent since February 2013. The leading index measures the economic performance of the region six months ahead. While the index increased 12.6 percent since its lowest level in March 2009, the increase over the one-year period ending in February suggests that the region's economy will grow at a very modest rate over the first half of this year.

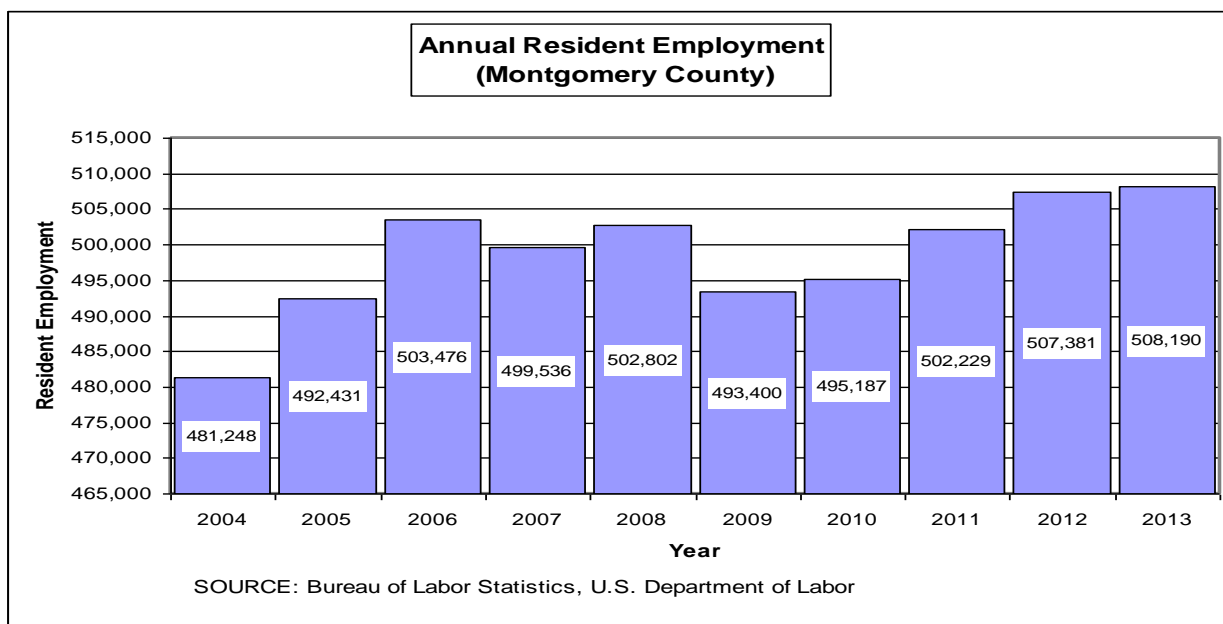


MONTGOMERY COUNTY ECONOMIC INDICATORS

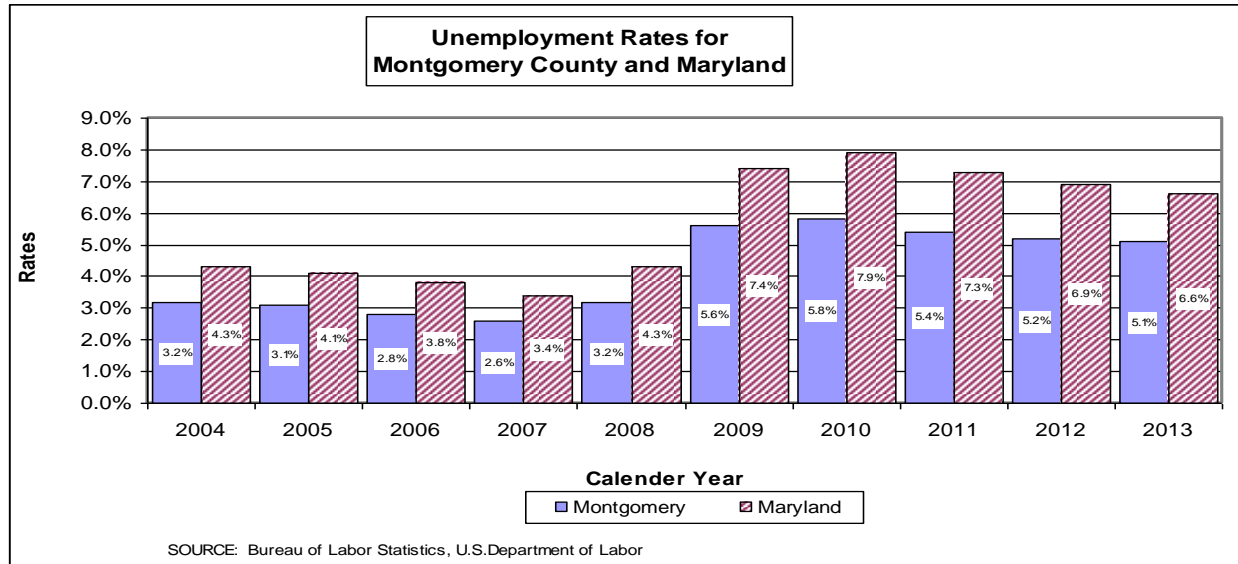
Montgomery County's economy experienced mixed performance during the first quarter of this year. The reasons for a positive performance were a decline in the unemployment rate, an increase in the median sales price for existing homes, and strong residential construction growth. The negative performance include a decline in existing home sales and very little growth in resident employment.

Employment Situation

Based on data from the Maryland Department of Labor, Licensing and Regulation (DLLR) and the Bureau of Labor Statistics, U.S. Department of Labor, average monthly resident employment (labor force series and not seasonally adjusted) for the first quarter in Montgomery County increased a modest 182 from the first quarter of 2013 ($\uparrow 0.04\%$) the same as the rate for the Bethesda-Rockville-Frederick metropolitan division and the lowest one quarter increase since resident employment began its increase in the second quarter of 2010. On an annual basis, resident employment stood at 508,190 in 2013 compared to 507,381 during the previous year – an increase of 0.2 percent.



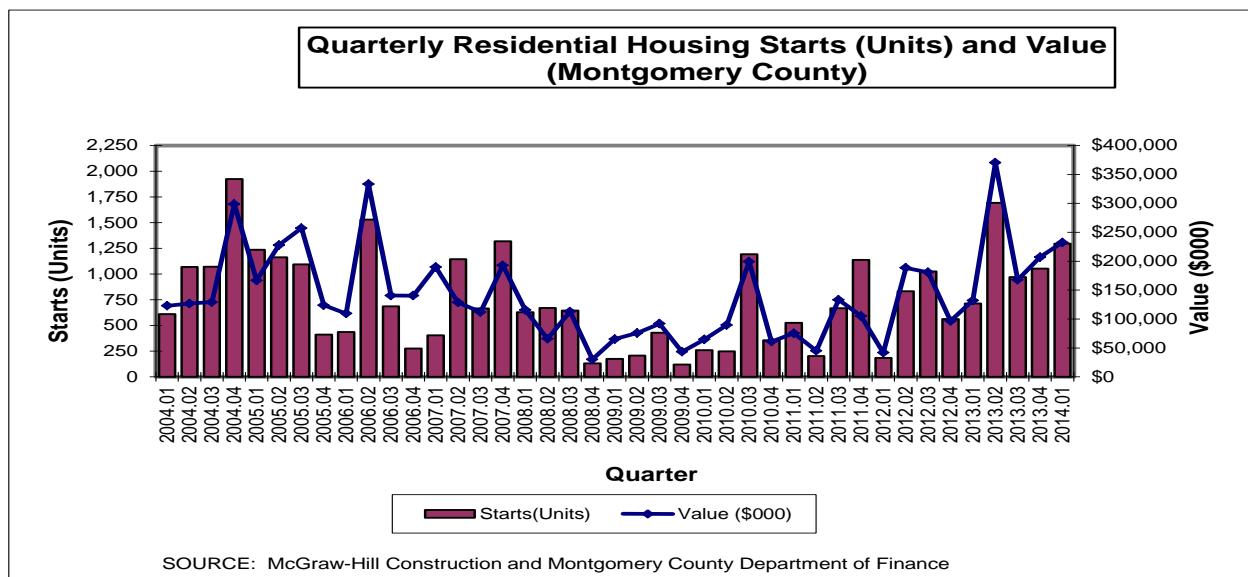
However, the County's average monthly unemployment rate during the first quarter declined to 4.4 percent compared to the annual rate of 5.2 percent in the first quarter of 2013. Throughout the calendar year 2013, the County's unemployment rate remained one of the lowest in the State and averaged 1.6 percentage points below the State's average in 2013 and averaged 1.4 percentage points below the State's average over the past ten years.



While the annual unemployment rate has remained at or above the 5.0 percent level for the past five calendar years, it has declined steadily since its peak in 2010. The decline has been attributed to an increase in resident employment and a decline in the number of unemployed since 2010. Employment grew by over 13,000 during the three-year period while the number of unemployed declined by nearly 3,700 over the same period.

Construction Activity

Residential construction experienced strong performance during the first quarter. The total number of new construction starts (residential units) increased 81.8 percent compared to the first quarter of 2013. Strong residential construction starts is attributed to multifamily units (↑123.1%) and single-family units (↑33.2%) and added a total value \$100.2 million in the first quarter – an increase of 75.9 percent over the first quarter 2013.

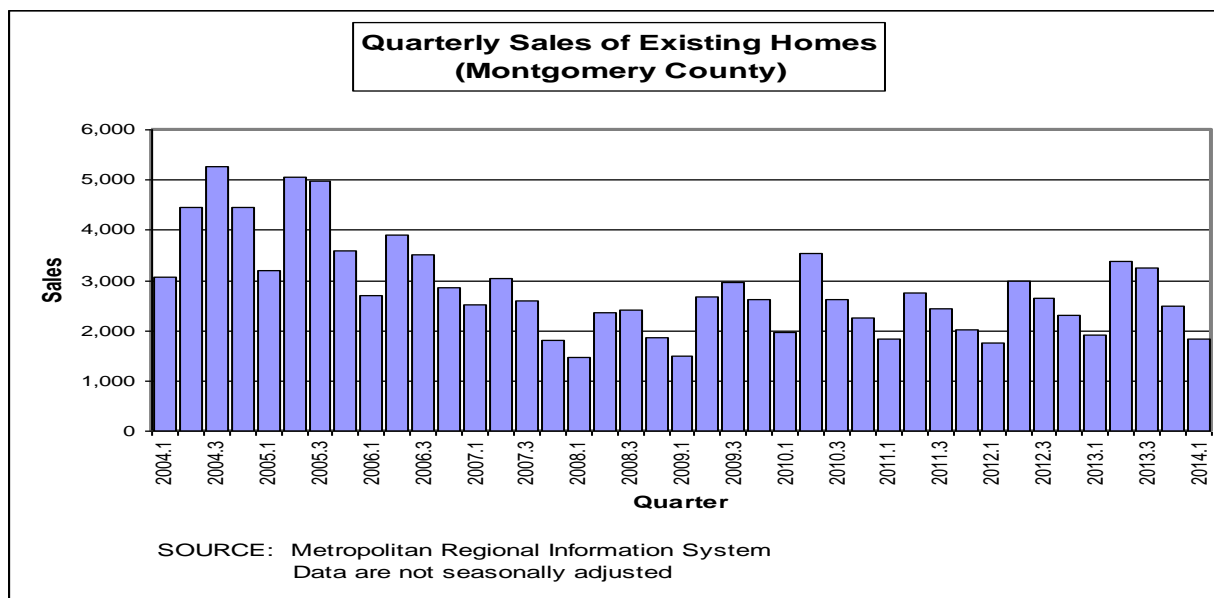


During the first quarter of 2014, the number of non-residential starts (projects) increased 50.0 percent but the total value decreased from \$127.9 million to \$50.9 million (↓60.2%). Because of the decline in the value of non-residential projects during the first quarter, construction starts added a total value of only \$171.5 million to the property tax base – a decrease of 13.5 percent from the first quarter of 2013.

At the same time that the total number of construction starts increased during the first quarter, construction costs were down 0.1 percent compared to costs during the first quarter of last year. The construction cost index developed by the *Engineering News Record* (ENR) for the Baltimore area increased 5.1 percent in 2010, 3.0 percent in 2011, 3.5 percent in 2012, and 5.2 percent in 2013. Therefore, while construction activity increased during the first quarter, that increase was not attributed to inflation in construction costs but rather to real economic activity in residential construction.

Residential Real Estate

During the first quarter of this year, existing home sales decreased 4.0 percent following increases of 7.9 percent during the first quarter of 2013, 13.3 percent during the second quarter, 22.9 percent during the third quarter, and 8.2 percent during the fourth quarter of 2013. The decrease during the first quarter after strong growth throughout 2013 can be attributed to rising mortgage interest rates and increases in home prices. Median sales prices for existing homes increased 3.4 percent during the first quarter compared to the first quarter of last year. Median sales prices have increased the past eight quarters with a range between 3.4% and 10.4%.



Retail Sales

Using sales tax receipts as a measure of retail sales activity in the County, sales of durable and nondurable goods decreased 0.9 percent during the first quarter of this year. Purchases of

nondurable goods, which include food and beverage, apparel, general merchandise, and utilities and transportation, increased 0.8 percent during this period while sales of durable goods were down 5.1 percent. The increase in nondurable goods purchases was largely attributed to the increase in utilities and transportation (↑12.2%) while the decrease in purchases of durable goods was attributed to a decline in sales of furniture and appliances (↓14.7%) and building and industrial supplies (↓6.0%) both indicative of a weaker housing market during the first quarter.

Based on sales tax data between calendar years 2004 and 2013, first quarter revenues represented between 20.0 percent and 23.5 percent of total revenues with a ten-year average of 22.6 percent. Finally, comparing the percent changes from first quarter to first quarter with the annual percent changes, first quarter receipts provide an indication of retail sales for the entire calendar year. As such, one could expect very modest retail sales during the remainder of 2014.

CONCLUSION

The major economic indicators confirm that the County's economy experience mixed performance during the first quarter of this year. The monthly unemployment rate for the first quarter declined to 4.5 percent from 5.3 percent during the first quarter of 2013. Employment measured by households experienced a very modest gain. Residential construction improved with the construction of single-family homes up 123.1 percent and multi-family units up 81.8 percent. Sales of existing homes decreased but median sales prices increased during the first quarter compared to the first quarter of last year. The overall inflation rate in the region remained subdued but retail sales, particularly for purchases of durable goods, were down.

SELECTED ECONOMIC INDICATORS	Reporting Period	Current Period	Prior Year's Period	Year To-Date		Annual
				2014	2013	2013
Leading Indicators						
National	Mar. '14	0.8%		6.2%	-0.9%	2.6%
Washington MSA	Feb. '14	1.7%		5.0%	-0.7%	-0.5%
Coincident Indicators						
National	Mar. '14	0.2%		2.8%	1.3%	2.1%
Washington MSA	Feb. '14	-2.1%		-0.5%	5.8%	1.7%
Consumer Confidence Index						
National	Apr. '14	-1.9%		25.9%	-5.2%	9.2%
South Atlantic Region	Apr. '14	10.4%		29.3%	0.7%	7.3%
Consumer Sentiment (University of Michigan)	Apr. '14	5.7%		6.9%	1.2%	3.5%
Consumer Price Index						
All Items (nsa)						
National	Mar. '14	1.5%		1.4%	1.7%	1.5%
Washington - Baltimore CMSA	Mar. '14	1.6%		1.7%	1.6%	1.5%
Core CPI (nsa)						
National	Mar. '14	1.7%		1.6%	1.9%	1.8%
Washington - Baltimore CMSA	Mar. '14	1.9%		1.8%	1.9%	1.8%
Retail Trade						
National (sales - nsa)	Mar. '14	2.6%		2.2%	-4.2%	3.3%
Maryland (sales tax)(1)	Mar. '14	3.3%		-0.4%	-4.2%	1.8%
Montgomery County (sales tax)(1)	Mar. '14	3.4%		-1.0%	-1.4%	0.2%
Employment						
Maryland (labor force data - nsa)	Mar. '14	2,915,293	2,912,743	2,906,470	2,899,598	2,921,931
- Percent Change		0.1%		0.2%		0.4%
Bethesda-Frederick-Gaithersburg (labor force data)	Mar. '14	627,287	627,575	627,057	626,831	629,684
- Percent Change		0.0%		0.0%		0.2%
Montgomery County (labor force data)	Mar. '14	506,255	506,488	506,070	505,888	508,190
- Percent Change		0.0%		0.0%		0.2%
Montgomery County (QCEW)	Sept. '13	454,271	454,195	451,070	449,168	450,880
- Percent Change		0.0%		0.4%		0.7%
Unemployment						
Maryland (nsa)	Mar. '14	5.9%	6.7%	6.0%	7.1%	6.6%
Bethesda-Frederick-Gaithersburg (nsa)	Mar. '14	4.6%	5.2%	4.6%	5.4%	5.2%
Montgomery County (nsa)	Mar. '14	4.5%	5.1%	4.4%	5.2%	5.1%
Construction						
Construction Starts - Montgomery County						
Total (\$ thousands)	Mar. '14	\$108,562	\$87,159	\$283,137	\$260,016	\$1,595,054
- Percent Change		24.6%		8.9%		20.2%
Residential (\$ thousands)	Mar. '14	\$91,991	\$60,409	\$232,276	\$132,079	\$823,039
- Percent Change		52.3%		75.9%		58.7%
Non-Residential (\$ thousands)	Mar. '14	\$16,571	\$26,750	\$50,861	\$127,937	\$772,015
- Percent Change		-38.1%		-60.2%		-4.5%
Building Permits (Residential)						
Maryland	Mar. '14	1,059	1,732	3,604	3,819	18,138
- Percent Change		-38.9%		-5.6%		23.8%
Montgomery County (units)	Mar. '14	237	197	1,225	453	3,514
- Percent Change		20.3%		170.4%		-10.9%
Building Permits (Non-Residential)						
Montgomery County	Mar. '14	125	175	358	450	2,060
- Percent Change		-28.6%		-20.4%		-6.3%
Construction Cost Index						
Baltimore	Mar. '14	6,941.60	6,987.03	6,935.61	6,944.17	6,935.72
		-0.7%		-0.1%		5.2%
Real Estate						
Case-Shiller Home Price Index®						
	Feb. '14	203.45	186.56	203.39	187.00	198.40
		9.1%		8.8%		6.9%
Maryland						
Sales	Mar. '14	4,352	4,571	11,158	11,349	63,556
- Percent Change		-4.8%		-1.7%		12.4%
Median Price	Mar. '14	\$245,891	\$241,450	\$240,953	\$229,621	\$261,153
- Percent Change		1.8%		4.9%		6.6%
Montgomery County						
Sales	Mar. '14	709	826	1,829	1,905	11,406
- Percent Change		-14.2%		-4.0%		13.0%
Average Price	Mar. '14	\$494,869	\$484,775	\$481,404	\$452,615	\$500,316
- Percent Change		2.1%		6.4%		7.5%
Median Price	Mar. '14	\$375,000	\$375,000	\$375,000	\$362,500	\$400,000
- Percent Change		0.0%		3.4%		9.0%
Average Days on the Market	Mar. '14	54	58	57	63	46

NOTES:

(nsa): not seasonally adjusted

(QCEW): Quarterly Census of Employment and Wages

(saar): seasonally adjusted at annual rate

(1): Data include miscellaneous and assessment collections.

(n.m.): not meaningful